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Decision 03-06-044 June 19, 2003

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

In the Matter of the Application of Verizon Advanced Data Inc. (U 6454 C) to Transfer Intrastate Advanced Data Services Assets and California Customer Base, Withdraw Service and Cancel its CPCN.	Application 01-11-014 (Filed November 13, 2001)
Application of Verizon California Inc. (U 1002-C) for Approval to Transfer Intrastate Advanced Data Service Assets to Verizon Advanced Data Inc.	Application 00-09-028 (Filed September 1, 2000)

OPINION GRANTING APPLICATION 01-11-014, BIFURCATING PROCEEDING, AND GRANTING MOTION TO WITHDRAW APPLICATION 00-09-028

I. Summary

In this decision, we grant Application (A.) 01-11-014 of Verizon Advanced Data Inc. (VADI) to transfer its advanced data services assets and reintegrate with Verizon California Inc. (Verizon). We also grant Verizon's motion to withdraw its earlier filed application to transfer intrastate advanced data service assets to VADI (A.00-09-028) on the ground that subsequent events have superseded the need to act on the application given Verizon's decision not to maintain advanced services in the separate VADI affiliate. We consolidate both applications, and bifurcate A.01-11-014 into two phases, Phase 1 and Phase 2. In Phase 1, we grant the application to transfer VADI assets back to Verizon, but

reserve Phase 2 for consideration of the competitive issues raised in a protest to the application.

II. Background

Verizon created VADI in response to a condition imposed by the Federal Communications Commission's (FCC) order approving the merger of Bell Atlantic Corporation and GTE Corporation.[1] This merger created the entity we now know as Verizon. The merger condition required that Verizon transfer its advanced services,[2] such as its digital subscriber line (DSL) service, to a separate affiliate to protect competitors against anti-competitive behavior:

> [T]o ensure that competing providers of advanced services receive effective, nondiscriminatory access to the facilities and services of the merged firm's incumbent [local exchange carriers] that are necessary to provide advanced services. Because the merged firm's own separate affiliate will use the same processes as competitors, wait in line for collocation space, buy the same inputs used to provide advanced services, and

[1] *In the Matter of GTE Corporation, Transferor, and Bell Atlantic Corporation, Transferee, for Consent to Transfer Control*, CC Docket No. 98-184, *Memorandum Opinion and Order,* FCC 00-221 (rel. June 16, 2000) ¶ 260 ("Bell Atlantic and GTE will create, prior to closing the merger, one or more separate affiliates to provide all advanced services in the combined Bell Atlantic/GTE region on a phased-in basis. The structural and non-structural safeguards we adopt today will make engaging in anticompetitive misconduct more difficult.").

[2] Advanced services include, in Verizon's case, switched multimegabit data service (SMDS), Frame Relay, asynchronous transfer mode (ATM) service, multi-media data service (MMDS), transport LAN connection (TLC), and Digital Subscriber Line (DSL) service. According to the FCC, "'Advanced Services' means intrastate or interstate wireline telecommunications services, such as ADSL, IDSL, xDSL, Frame Relay, and asynchronous transfer mode (ATM) that rely on packetized technology and have the capability of supporting transmissions speeds of at least 56 kilobits per second in both directions." *Id.,* Appendix D, "Conditions for Bell Atlantic/GTE Merger," ¶ 2.

> pay an equivalent price for facilities and services, the condition should ensure a level playing field between Bell Atlantic/GTE and its advanced services competitors.[3]

In A.00-09-028, Verizon applied to this Commission for authority to transfer its intrastate advanced data assets to VADI. Thereafter, however, a federal appellate court ruled that the FCC's separate affiliate requirement would not mitigate the anti-competitive problems that had concerned the FCC. In *Ass'n of Communications Enterprises v. FCC*, 235 F.3d 662 (D.C. Cir. 2001), the court reversed the FCC decision that incumbent local exchange carriers (ILECs) need not resell advanced services to competitors so long as the services are provided by a separate affiliate.[4]

Because resale of advanced services was something the ILECs were attempting to avoid, the D.C. Circuit's elimination of ILEC protection from the resale obligation motivated Verizon to abandon its plans to house advanced services in a separate affiliate.[5] Verizon therefore filed a motion to withdraw A.00-09-028, and VADI filed A.01-11-014 seeking permission to transfer advanced services back to Verizon. VADI had to file A.01-11-014 because it provided advanced services for a time under a revocable license from Verizon, as we discuss below. This decision resolves both issues.

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[3] *Id.*, ¶ 261.

[4] After the D.C. Circuit issued its decision, A.00-09-028 was stayed at Verizon's request in order to give Verizon time to consider its options. Ultimately, Verizon filed a motion to withdraw A.00-09-028, which we resolve here.

[5] Pacific Bell, in contrast, seeks to maintain its advanced services in a separate affiliate despite the D.C. Circuit's decision. A.02-07-039.

Various parties[6] protested A.01-11-014, alleging that the application does not provide sufficient information to allow an informed response and suggesting that the Commission impose conditions on the VADI transfer. They state that their proposed conditions, if adopted, would protect competitive local exchange carriers (CLECs) after VADI's reintegration into Verizon. They urge consideration of their issues either here in A.01-11-014, or in the Commission's line-sharing proceeding, Rulemaking (R.) 93-04-003/Investigation (I.) 93-04-002.

The protesting parties express concern that if VADI is not maintained as a separate affiliate, it will receive preferential treatment from Verizon, such as the ability to reserve space in central offices and remote terminals, at the expense of CLECs. They claim that in the Commission's line-sharing proceeding, a Verizon witness gave them cause for such concern: "Verizon is unwilling to provide [CLECs] with the same type of access to pre-ordering, ordering, provisioning, maintenance and repair, and billing available to Verizon itself, because [the witness claimed that] '[t]he FCC has not mandated that Verizon provide [a CLEC] the same type of access . . . that is available to itself.'"[7]

The Commission's Office of Ratepayer Advocates (ORA) supports A.01-11-014 and the reintegration of the advanced services assets from VADI to Verizon "to ensure that the jurisdiction of the Commission is preserved and to ensure that the Commission has the capacity to effectively regulate Verizon's

[6] The protesting parties are Covad Communications Company (Covad), WorldCom, Inc. (WorldCom) and The Utility Reform Network (TURN). These parties did not protest A.00-09-028.

[7] *Protest of Covad, . . . WorldCom, . . . and . . . TURN [to A.01-11-014],* filed Dec. 17, 2001, at 7 (citation omitted).

service to the public." ORA does not propose conditions for approval of the transfer.[8]

ORA protested A.00-09-028 on the ground that the application did not address whether VADI had a certificate of public convenience and necessity (CPCN), was vague, and ignored the impact of the transfer on the quality of service for Verizon's basic service customers. Since Verizon is no longer pursuing A.00-09-028, we consider ORA's protest to be moot.

III. Discussion

A. Jurisdiction

There is a threshold question of the extent of our jurisdiction over advanced services. While VADI has already conceded that we have jurisdiction to decide A.01-11-014 by virtue of filing its application, it is important to note that in A.00-09-028, Verizon has claimed that we lack jurisdiction over DSL, currently the most commercially viable advanced service the ILECs offer.

In ruling on the scope of A.00-09-028, the Assigned Commissioner addressed this issue, noting that this Commission has jurisdiction to consider the effect of Verizon's VADI affiliate on competition. We quote and adopt the Commissioner's views, incorporated into the A.00-09-028 scoping memo, in their entirety for purposes of this Section 851 review:

> While Verizon asserts the Commission lacks jurisdiction over DSL, we agree with ORA that the authority Verizon cites is distinguishable. Verizon's position is that the FCC has jurisdiction over DSL pricing because all but a *de minimis* amount of DSL traffic is interstate (the so called "10% rule").

[8] *Response of the Office of Ratepayer Advocates to the Questions of Administrative Law Judge Sarah Thomas Regarding A.00-09-028 and A.01-11-014,* filed May 24, 2002, at 1.

Thus, Verizon claims, this Commission has no authority to determine the effects on ratepayers of a transfer of DSL assets to an unregulated affiliate.[9] Verizon concedes this transfer will occur, but takes the position that neither this Commission nor the FCC need approve it.[10]

Even if we do not set prices for DSL, we have authority to consider the effects of the DSL transfer on Verizon's remaining California consumers. As ORA states,

> nothing in the GTE DSL Tariff Order holding that the FCC has jurisdiction over the rates charged for DSL service preempts the California Commission from considering whether to approve or disapprove the transfer of the DSL service assets at issue here.[11]

As ORA further states, Section 253 of the 1996 Telecommunications Act (96 Act) provides that states can impose requirements "necessary to preserve and advance universal service, protect the public safety and welfare, ensure the continued quality of telecommunications services, and safeguard the rights of consumers."[12] If, as ORA alleges, the DSL asset transfer presents risks to service

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[9] *Brief of Verizon California Inc. on Jurisdiction Over DSL Services and Valuation of Advanced Services Assets*, filed December 6, 2000 in A.00-09-028 (Verizon Jurisdiction/Valuation Brief), at 2, citing *Matter of GTE Telephone Operating Cos., GTOC Tariff No. 1, GTOC Transmittal No. 1148*, CC Docket No. 98-79, (rel. Oct. 30, 1998) ("GTE DSL Tariff Order"). The FCC held there that "GTE's DSL Solutions-ADSL service offering is an interstate service that is properly tariffed at the federal level." *Id.* at ¶ 16.

[10] *See* Transcript of November 15, 2000 PHC in A.00-09-028, at 6:14-7:8.

[11] *Response of the Office of Ratepayer Advocates to the Brief of Verizon California Inc., on Jurisdiction Over DSL Services and Valuation of Advanced Services Assets,* filed January 10, 2001 in A.00-09-028 (ORA Response Jurisdiction/Valuation Brief), at 3.

[12] 47 U.S.C. § 253(b).

quality for Verizon's remaining services, or to competition, this Commission retains jurisdiction to address such issues.

Moreover, as ORA asserts, Public Utilities Code § 851 is entirely consistent with the federal law. Section 851 provides that,

> No public utility . . . shall sell, lease, assign, mortgage or otherwise dispose of or encumber the whole or any part of its . . . property necessary or useful in the performance of its duties to the public . . . .

If the DSL transfer would affect Verizon's ability to perform its duties to ratepayers – by, for example, leaving Verizon short of service representatives, installers, or others – the Commission's § 851 review should consider that consequence.

ORA also points out that DSL service uses the local loop and is sold only as a bundled service with the local loop: "Clearly, as part of Verizon's local loop facilities, Verizon's DSL assets are necessary and useful in the provision of service to the public, as set forth in Section 851."[13] We agree.

ORA further points out that the Commission has previously held that,

> When, as here, the transactions are with a corporate affiliate, the Commission's [Section 851] review also includes consideration of whether the transaction may have anti-competitive effects or result in cross-subsidization of non-regulated entities.[14]

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[13] ORA Response Jurisdiction/Valuation Brief, at 7.

[14] *In the Matter of Pacific Bell,* D.98-07-006, 1998 Cal. PUC LEXIS 547, at *6.

We agree with ORA that this reasoning applies with equal force here, and gives us the power to ensure that Verizon does not benefit unduly *vis-à-vis* its competitors from the asset transfer.

Furthermore, when the FCC approved the Bell Atlantic-GTE merger leading to Verizon's creation, and created the separate data affiliate requirement, the FCC stated that the condition was "not intended to limit the authority of state commissions to impose or enforce requirements that go beyond those adopted in this Order."[15]

In New York, the Public Service Commission recently considered a similar application by Bell Atlantic. In that case, Bell Atlantic had petitioned for approval of the transfer of certain assets associated with advanced services to a separate data affiliate. There, too, Bell Atlantic argued that the New York Commission did not have jurisdiction to examine the assets because the FCC had exclusive jurisdiction over them. The New York Public Service Commission rejected Bell Atlantic's efforts to avoid regulatory review.[16] Thus, our decision here is not without precedent in other states.

In our view, the Commission is asserting jurisdiction not to consider whether VADI customers will be harmed or otherwise affected by the transfer, but whether the California customers left behind at Verizon will be harmed. Verizon nowhere contends that the FCC will ensure that such customers are protected. Indeed, it does not even plan to submit the DSL asset transfer to the FCC for approval.

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[15] *In Re Application of GTE Corporation, Transferor, and Bell Atlantic Corporation, Transferee, Memorandum Opinion and Order,* CC Docket No. 98-184, adopted June 16, 2000, ¶ 254.

[16] *Petition of Bell Atlantic – New York for Approval of the Transfer of Certain Assets Associated with Advanced Services to Bell Atlantic Network Data Inc., a Structurally Separate Affiliate,* Case 00-C-0725, 2000 N.Y. PUC LEXIS 652 (2000).

> Thus, we must perform this role here, or at the very least, ensure development of a record for Commission consideration. The valuation of DSL assets, and the effect on the public interest of their transfer, are issues within the scope of this proceeding.[17]

B. Motion to Withdraw A.00-09-028

We grant Verizon's motion to withdraw A.00-09-028. No party has opposed the withdrawal, and given ORA's concerns about our ability to regulate Verizon's advanced services if they are outside the ILEC, we find the withdrawal to be in the public interest.

In D.92-04-027,[18] we made clear that an applicant may not always withdraw a proceeding that has made substantial progress through this Commission. To allow withdrawal as of right in such a case could allow a party to dismiss an application when it appears it is about to receive an unfavorable decision. Where, however, the Commission was persuaded that a utility's desire to withdraw the application was due to the uncertainties in the regulated industry in general and not because its application was likely to fail, we allowed withdrawal.[19]

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[17] *Scoping Memo and Ruling of Assigned Commissioner and Administrative Law Judge* in A.00-09-028, dated Jan. 25, 2001, at 5-8.

[18] 43 CPUC 2d 639 (1992) ("We need not speculate on the possible circumstances which would cause us to regard dismissal or withdrawal as no longer a matter of right. It is sufficient that we indicate that submission of a matter upon an evidentiary record and obtaining a proposed decision within the meaning of Section 311(d) involve steps which clearly make termination a matter of the Commission's discretion.")

[19] D.94-05-024, 54 CPUC 2d 456.

There is no indication in this proceeding that Verizon is motivated to withdraw A.00-09-028 because it fears an adverse decision on the merits, and no party has protested the withdrawal or claimed that Verizon seeks withdrawal for nefarious reasons. Thus, withdrawal is appropriate in this case.

Moreover, with the withdrawal, and the approval of VADI's application to reintegrate its advanced services assets into Verizon, any concern over the extent of our jurisdiction over such assets raised by their separateness from Verizon will disappear. We also find moot the issues ORA raised in its protest to A.00-09-028. Therefore, we dismiss A.00-09-028 in its entirety with prejudice.

C. Resolution of A.01-11-014

1. Competitive Issues

We do not believe we must first resolve the issues the protesting parties raise in A.01-11-014 before allowing VADI to transfer advanced services back to Verizon. Therefore, we will grant the transfer requested in A.01-11-014, but bifurcate the proceeding and reserve the protesting parties' issues for a later phase of the proceeding.

There is regulatory uncertainty at the federal level as to whether ILECs will be required to offer CLECs line-sharing over fiber-fed loops. Thus, we are unable at this time to determine what FCC policy is regarding some of the competitive issues the protesting parties raise, and whether the FCC will leave room for state commissions to impose competitive obligations on ILECs in their

provision of advanced services.[20] To preserve scarce Commission resources and ease logistics, we believe it prudent to await the FCC's decision on this question

[20] Regardless of the FCC's actions, this Commission may well retain state law authority in this area.

so as to help us determine whether to consider imposing various line-sharing obligations, and in what forum (*i.e.*, the line-sharing proceeding or A.01-11-014) to impose them.

On February 23, 2003, the FCC indicated its intent to change the rules regarding fiber-fed loops, stating in a press release that it would soon adopt a new framework for ILECs' "obligations to make elements of their networks available on an unbundled basis to new entrants" in order to "provide incentives for carriers to invest in broadband network facilities":

> Broadband Issues – The Commission [in its anticipated order] provides substantial unbundling relief for loops utilizing fiber facilities: 1) the Commission requires no unbundling of fiber-to-the-home loops; 2) the Commission elects not to unbundle bandwidth for the provision of broadband services for loops where incumbent LECs deploy fiber further into the neighborhood but short of the customer's home (hybrid loops), although requesting carriers that provide broadband services today over high capacity facilities will continue to get that same access even after this relief is granted, and 3) the Commission will no longer require that line-sharing be available as an unbundled element. The Commission also provides clarification on its UNE pricing rules that will send appropriate economic signals to carriers.

Whether and the extent to which DSL and other advanced services will be affected by the FCC decision remains to be seen. We believe it is best to resolve the issues the protesting parties raise in A.01-11-014 at a later time, when we have more regulatory certainty regarding the ILECs' obligations in this area. Therefore, we bifurcate this proceeding into two phases.

In Phase 1, we grant VADI's application to transfer advanced services assets back to Verizon. In the second phase, Phase 2, we may consider

whether we should impose any conditions on Verizon in order to ensure it treats competitors fairly in connection with its advanced services. We take this approach because it is most likely that we ultimately will resolve the issues the A.01-11-014 protesting parties raise in the line-sharing proceeding, R.93-04-003/I.93-04-002, since that proceeding is concerned with an array of competitive issues affecting ILECs' competitors. If it later appears that it is more appropriate for us to handle the protesting parties' concerns in this proceeding, we or the assigned Commissioner or assigned ALJ will provide such clarification.

We stay commencement of Phase 2 of A.01-11-014 until after the FCC issues its order related to the February 23, 2003 press release. The Commission, assigned Commissioners or assigned ALJ may issue an order or ruling in A.01-11-014 and/or R.93-04-003/I.93-04-002 clarifying where the competitive issues should be raised. In addition, any party may ask us to lift the stay of Phase 2 and/or resolve the competitive issues in this proceeding, A.01-11-014. If we do not lift the stay of Phase 2 within one year of the effective date of this decision, A.01-11-014 will be closed automatically.

2. Merits of VADI's Application

We grant VADI's application to transfer advanced services back to Verizon. VADI and Verizon state that in conjunction with the transfer of assets, they will file an advice letter reintegrating VADI tariffs into those of Verizon California. We agree that Verizon should make this filing and also file and serve it in this proceeding. Verizon shall also file and serve a compliance filing in this proceeding containing an explanation of the accounting and ratemaking treatment it proposes be employed. It shall identify 1) the specific accounts from the FCC Part 32 Uniform System of Accounts that it will use to classify the assets, 2) the proposed ratemaking treatment of the assets (*e.g.*, whether assets will be

allocated to federal jurisdiction, state jurisdiction, or a combination), 3) whether it will treat the assets above-the-line or below-the line, 4) the proposed NRF service categorization (Category I, II or III) of the advanced services, 5) the amount of assets subject to the license agreement between VADI and Verizon and the reimbursement paid to Verizon for the length of the license agreement, 6) the amount of collocation space transferred to VADI while it operated independently and the reimbursement paid to Verizon for collocation, 7) whether VADI valued the assets it purchased and is now reintegrating at "original cost."

The explanation of the accounting and ratemaking treatment shall also specify how Verizon intends to track the operation of the advanced services and its associated assets, liabilities, revenues and costs. Verizon shall include in its compliance filing the change in its organization chart from before and after the re-integration of VADI into Verizon. Parties may protest the advice letter filing or the compliance filing.

VADI will return to Verizon the customers whose services have been transferred from Verizon to VADI. Upon completion of these steps, VADI will seek cancellation of its CPCN.[21] VADI states that the merger is appropriate because it reduces customer confusion and returns Verizon's operations to the basic model existing before the FCC entered its merger order.

Verizon also correctly points out that it is not precluded by FCC order from transferring VADI assets back to Verizon. Indeed, the FCC has approved the reintegration on the ground that vacating the structural separation

[21] VADI's A.01-11-014 Application at 2.

requirement "is in the public interest and furthers the goal of promoting deployment of advanced services."[22]

However, we are concerned about two additional issues: the effect of the transfer on end-user customers, and the financial impact of the transfer for ratepayers. First, we believe there is potential for customer confusion unless they receive notice of the transfer back to Verizon of advanced services assets Verizon transferred to VADI under a revocable license. Therefore, we will require that as a condition of the transfer, Verizon and VADI jointly notify customers of the transfer and make clear that these customers are not required to take advanced services from Verizon/VADI except to the extent that customers are subject to a term commitment pursuant to a contract or under applicable tariff. Verizon and VADI shall prepare a joint notice explaining this decision to customers, submit it to the Commission's Public Advisor for review and approval prior to mailing, and mail the notice to all customers - as a separate mailing or a bill insert - at least 10 business days before effecting the asset transfer.

Second, it is unclear whether the transfer will have any financial impact on Verizon's regulated operations or ratepayers. VADI states that pending approval of A.00-09-028 (the application we dismiss in this decision), VADI "utilized Verizon California's assets in the interim pursuant to a revocable license that would not be subject to approval under [Pub. Util. Code] Section 851." VADI cited the Commission's General Order (GO 69-C) as support for its claim. We agree that GO 69-C allows revocable licenses without Commission authorization in certain narrow instances, so long as the transaction at issue is

[22] *In the Matter of GTE Corporation, Transferor, and Bell Atlantic Corporation, Transferee, for Consent to Transfer Control,* CC Docket No. 98-184, *Order,* ¶ 6 (rel. Sept. 26, 2001).

temporary in nature and can be easily undone. We do not find that Verizon violated § 851 in allowing VADI to operate under a revocable license before Verizon secured approval under § 851 for an irrevocable transfer of its advanced services assets. However, we believe Verizon should include information about the effect of the transfer in its compliance filing.

Moreover, there may be a financial impact that indirectly affects ratepayers by virtue of the transfer of advanced services assets back to Verizon. VADI intends to transfer the services to Verizon based on net book value. However, when ORA protested A.00-09-028, the original application in which Verizon proposed to transfer assets to VADI, ORA claimed that valuation at book value was inadequate, and that the transferred assets should be valued as a (presumably more valuable) "going concern."

At that time, ORA contended that to value the assets at their net book value would underestimate the amount of money Verizon's regulated operations should receive as a result of the transfer, because such a valuation methodology would value assets piece by piece. The value of those assets as a unit - the going concern value of them - was greater than the sum of the pieces, ORA contended: "The operating components should be valued in their entirety, as an on-going enterprise with significant market capitalization, and not piece-by-piece as one would for a liquidation sale."[23]

ORA claimed that the "going concern" valuation approach was based on fair market value, and thus was within the "higher of net book value or fair market value" rubric relevant to a valuation of the assets transferred.

[23] *Protest of the Office of Ratepayer Advocates*, filed in A.00-09-028 Oct. 20, 2000, at 5.

Because ORA has abandoned this claim here in not protesting A.01-11-014, we approve Verizon's method of valuing the assets. In its compliance advice letter filing, VADI may value the assets being transferred back to Verizon on a book value basis.

IV. Conclusion

For the foregoing reasons, we grant Verizon's motion to withdraw A.00-09-028. We bifurcate A.01-11-014 into two phases, but grant VADI's application to reintegrate advanced services into Verizon at this time. If we do not address the competitive issues the protesting parties raise in A.01-11-014 in our line-sharing proceeding, they may renew their request for consideration of those issues in Phase 2 of this proceeding.

V. Comment on Draft Decision

The draft decision of the ALJ in this matter was mailed to the parties in accordance with Section 311(g)(1) of the Public Utilities Code and Rule 77.7 of the Rules of Practice and Procedure. Comments were filed on June 9, 2003 and reply comments were filed on June 16, 2003.

Verizon/VADI, TURN, ORA and Covad commented on the draft decision. We modify the decision in part to take account of their concerns. We address the comments by issue.

Competitive Issues

We do not change our basic decision that we will deal with competitive issues at a later date, despite TURN's and Covad's opposition to this stance. We believe that by providing two potential forums to deal with TURN's and Covad's concerns – our line sharing docket and Phase 2 of this proceeding – we are ensuring that the Commission will have the opportunity to address all competitive issues the parties raise. We clarify that we are deferring

consideration of these issues not only because we are awaiting the FCC's Triennial Review order, but also to preserve scarce resources and ease logistics, as TURN suggests.

TURN and Covad also complain that the draft decision puts the onus entirely on the competitors to initiate a review of competitive issues in the future. To mitigate this concern, we change the process to make plain that the Commission, the assigned Commissioner or the assigned ALJ may initiate consideration of competitive issues in this proceeding or the line sharing proceeding, and that the onus need not be solely on the parties to commence the competitive review.

Jurisdiction

Verizon/VADI ask us to omit the discussion of jurisdiction in the draft decision, which we decline to do. As TURN points out, the issue is not moot by virtue of our dismissal of A.00-09-028 because TURN, MCI and Covad addressed the Commission's jurisdiction over DSL assets in their protest to A.01-11-014, which we adjudicate on the merits here. Moreover, we agree with TURN that we must dispel any suggestion that the Commission has no jurisdiction over DSL and that the FCC has exclusive jurisdiction in this area. Finally, we agree with TURN that we should modify the language of this decision to make clear that there may be other aspects of the jurisdiction question that we do not address here.

Advice Letter and Compliance Filings

Verizon/VADI ask that we allow for separate filings for tariffs and other compliance items. Neither TURN nor ORA object to such a change, and we adopt it.

ORA asks that we require Verizon in its compliance filing explaining the accounting and ratemaking treatment to specify how Verizon intends to track the operation of the advanced services and its associated assets, liabilities, revenues and costs, and include in its compliance filing the change in its corporate organization chart from before and after the reintegration. Verizon/VADI do not address this suggestion, but we find it reasonable and adopt it.

TURN asks that we have Verizon/VADI provide additional assurances as part of their compliance filing requirement: assurance that Verizon's ratepayers were not unduly burdened during the time VADI operated as a separate affiliate by allowing for inadequate reimbursement of Verizon central office space or assets used by VADI; demonstration that Verizon will not be harmed by the reintegration by overvaluation of the new assets acquired by VADI and brought back into the parent; proof that VADI was not given an unfair competitive advantage during the time it operated independently; and assurance that Verizon is not being given an unfair advantage vis-à-vis its competitors by incorrectly valuing the assets coming back into Verizon.

Verizon opposes TURN's proposed changes principally on the grounds that Verizon/VADI engaged in no anticompetitive activity and the dollar amount at stake is small. However, if Verizon/VADI are correct that they did nothing wrong, they should have no difficulty meeting the compliance filing requirements. We therefore agree with TURN in this regard and impose the additional compliance obligations. The parties will have a right to protest the advice letter and compliance filings.

We also agree with TURN that Verizon/VADI shall file and serve all compliance and advice letter filings in this docket as well as on the normal advice letter service lists.

Notice to Customers

Verizon/VADI ask us to omit the notice to customers on the ground it will "patronize" and confuse them. We do not agree that informing customers of a change in their service and of rules relevant to the change is patronizing or confusing, and we decline Verizon/VADI's suggestion. We agree with Verizon/VADI's suggestion – and TURN and ORA do not oppose it – that the notice should be modified to take into account customers with a contract or taking a tariffed rate that precludes them from changing carriers. Thus, the portion of the notice informing customers that they are not required to take advanced services from Verizon/VADI should be qualified with the following language: "except to the extent that customers are subject to a term commitment pursuant to a contract or under the applicable tariff."

VI. Assignment of Proceeding

Carl Wood is the Assigned Commissioner and Sarah R. Thomas is the assigned ALJ in this proceeding.

Findings of Fact

1. In 2000, Verizon created VADI in response to a condition imposed by the FCC's order approving the merger of Bell Atlantic Corporation and GTE Corporation, which created the entity we now know as Verizon.

2. The merger condition required that Verizon transfer its advanced services, such as its DSL service, to a separate affiliate to protect competitors against anti-competitive behavior.

3. In 2001, the United States Court of Appeals for the D.C. Circuit ruled that the FCC's separate affiliate requirement would not mitigate the anti-competitive problems that had concerned the FCC.

4. The D.C. Circuit's elimination of ILEC protection from the resale obligation motivated Verizon to abandon its plans to house advanced services in a separate affiliate.

5. There is regulatory uncertainty at the federal level as to whether ILECs will be required to offer CLECs line-sharing over fiber-fed loops.

6. DSL is currently the most commercially viable advanced service the ILECs offer.

7. DSL service uses the local loop and is sold only as a bundled service with the local loop.

8. There is no indication in this proceeding that Verizon is motivated to withdraw A.00-09-028 because it fears an adverse decision on the merits.

9. No party has protested the withdrawal of A.00-09-028 or claimed that Verizon seeks withdrawal for nefarious reasons.

10. There is potential for customer confusion unless customers receive notice of the transfer of VADI assets back to Verizon.

11. The record does not adequately demonstrate whether the transfer will have any financial impact on Verizon's regulated operations or ratepayers.

12. VADI intends to transfer the services to Verizon based on net book value. However, when ORA protested A.00-09-028, the original application in which Verizon proposed to transfer assets to VADI, ORA claimed that valuation at book value was inadequate, and that the transferred assets should be valued as a (presumably more valuable) "going concern."

Conclusions of Law

1. Since Verizon is no longer pursuing A.00-09-028, ORA's protest is moot.

2. We need not first resolve the issues the protesting parties raise in A.01-11-014 before allowing VADI to transfer advanced services back to Verizon.

We most likely will deal with these issues in our line-sharing proceeding. It is therefore appropriate to approve the transfer now and leave room for later consideration of competitive issues in this proceeding if necessary.

3. It is best to resolve the issues the protesting parties raise in A.01-11-014 at a later time, when we have more regulatory certainty regarding the ILECs' obligations in this area, and to preserve scarce Commission resources and ease logistics.

4. VADI has conceded that we have jurisdiction to decide A.01-11-014 by virtue of filing its application.

5. In the context of this Section 851 proceeding, we have jurisdiction to consider the impact of A.00-09-028 and changes in Verizon's approach to advanced services on its regulated ratepayers. Even if we do not set prices for DSL, we have authority to consider the effects of the DSL transfer on Verizon's remaining California consumers. The Commission is asserting jurisdiction not to consider whether advanced services customers will be harmed or otherwise affected by the transfer, but whether Verizon's non-advanced services California customers will be harmed.

6. Section 253 of the Telecommunications Act of 1996 (96 Act) provides that states can impose requirements "necessary to preserve and advance universal service, protect the public safety and welfare, ensure the continued quality of telecommunications services, and safeguard the rights of consumers." If the DSL asset transfer presents risks to service quality for Verizon's remaining services, or to competition, this Commission retains jurisdiction to address such issues.

7. Nothing in the GTE DSL Tariff Order holding that the FCC has jurisdiction over the rates charged for DSL service preempts the California Commission from

considering whether to approve or disapprove the transfer of the DSL service assets at issue here.

8. Pub. Util. Code § 851 is not preempted by federal law governing regulation of advanced services. Section 851 provides that, "No public utility . . . shall sell, lease, assign, mortgage or otherwise dispose of or encumber the whole or any part of its . . . property necessary or useful in the performance of its duties to the public . . . ."

9. We have jurisdiction to ensure that Verizon does not benefit unduly *vis-à-vis* its competitors from the asset transfer.

10. When the FCC approved the Bell Atlantic-GTE merger leading to Verizon's creation, and created the separate data affiliate requirement, the FCC stated that the condition was "not intended to limit the authority of state commissions to impose or enforce requirements that go beyond those adopted in this Order."

11. Our decision here is not without precedent in other states. In New York, the Public Service Commission considered a similar application by Bell Atlantic. In that case, Bell Atlantic had petitioned for approval of the transfer of certain assets associated with advanced services to a separate data affiliate. There, too, Bell Atlantic argued that the New York Commission did not have jurisdiction to examine the assets because the FCC had exclusive jurisdiction over them. The New York Public Service Commission rejected Bell Atlantic's efforts to avoid regulatory review.

12. The withdrawal of A.00-09-028 is in the public interest.

13. ORA's concerns about our ability to regulate Verizon's advanced services if they are outside the ILEC disappear if A.00-09-028 is withdrawn.

14. An applicant may not always withdraw a proceeding that has made substantial progress through this Commission. To allow withdrawal as of right in such a case could allow a party to dismiss an application when it appears it is about to receive an unfavorable decision.

15. Withdrawal is appropriate where the utility's desire to withdraw the application is due to uncertainties in the regulated industry in general and not because its application is likely to fail.

16. Verizon is not precluded by FCC order from transferring VADI assets back to Verizon. Indeed, the FCC has approved the reintegration on the ground that vacating the structural separation requirement "is in the public interest and furthers the goal of promoting deployment of advanced services."

17. The transfer is appropriate because it reduces customer confusion and returns Verizon's operations to the basic model existing before the FCC entered its merger order.

18. General Order (GO 69-C) allows revocable licenses without Commission authorization in certain narrow instances, so long as the transaction at issue is temporary in nature and can be easily undone.

19. Verizon did not violate § 851 in allowing VADI to operate under a revocable license before Verizon secured approval under § 851 for an irrevocable transfer of advanced services assets, but should provide additional information in a compliance filing regarding the effect of the transfer.

20. It was not lawful for Verizon to transfer advanced services assets to VADI before we decided its application to do so.

O R D E R

IT IS ORDERED that:

1. We grant Application (A.) 01-11-014 of Verizon Advanced Data Inc. (VADI) to transfer its advanced data services assets and reintegrate with Verizon California Inc. (Verizon), subject to the conditions in Ordering Paragraph 3.

2. We grant Verizon's motion to withdraw its application to transfer intrastate advanced data service assets to VADI (A.00-09-028) on the ground that subsequent events have superseded the need to act on the application given Verizon's decision not to maintain advanced services in the separate VADI affiliate. We dismiss A.00-09-028 in its entirety with prejudice.

3. We consolidate A.01-11-014 and A.00-09-028 solely for the purposes of this decision, and bifurcate A.01-11-014 into two phases, Phase 1 and Phase 2. In Phase 1, we grant the application to transfer VADI assets back to Verizon, but reserve Phase 2 for consideration of the competitive issues raised in a protest to the application. If it later appears that it is more appropriate for us to handle the protesting parties' concerns in the line-sharing proceeding, R.93-04-003/I.93-04-002, we or the assigned Commissioner or assigned Administrative Law Judge (ALJ) will provide clarification at that time.

4. We stay commencement of Phase 2 of this proceeding until after the FCC issues its order related to the February 23, 2003 press release we discuss earlier in this decision. The Commission, assigned Commissioners or assigned ALJs may issue an order or ruling in A.01-11-014 and/or R.93-04-003/I.93-04-002 clarifying where the competitive issues should be raised. In addition, any party may ask us to lift the stay of Phase 2 and/or resolve the competitive issues in this proceeding, A.01-11-014. If we have not lifted the stay within one year of the effective date of this decision, A.01-11-014 will be closed automatically.

5. In conjunction with the transfer of assets, Verizon and VADI shall file an advice letter reintegrating VADI tariffs into those of Verizon California. Verizon and VADI shall also file and serve the advice letter in this proceeding. Parties may protest the advice letter filing in the normal course.

6. Verizon shall file and serve a compliance filing in this proceeding containing an explanation of the accounting and ratemaking treatment it proposes be employed. It shall identify 1) the specific accounts from the FCC Part 32 Uniform System of Accounts that it will use to classify the assets, 2) the proposed ratemaking treatment of the assets (*e.g.*, whether assets will be allocated to federal jurisdiction, state jurisdiction, or a combination), 3) whether it will treat the assets above-the-line or below-the line, and 4) the proposed NRF service categorization (Category I, II or III) of the advanced services, 5) the amount of assets subject to the license agreement between VADI and Verizon and the reimbursement paid to Verizon for the length of the license agreement, 6) the amount of collocation space transferred to VADI while it operated independently and the reimbursement paid to Verizon for collocation, and 7) whether VADI valued the assets it purchased and is now reintegrating at "original cost." The explanation of the accounting and ratemaking treatment shall also specify how Verizon intends to track the operation of the advanced services and its associated assets, liabilities, revenues and costs. Verizon shall include in its compliance filing the change in its organization chart from before and after the re-integration of VADI into Verizon. Parties may protest the compliance filing in accordance with the Commission's normal procedures for protesting advice letters.

7. VADI shall return to Verizon the customers whose services have been transferred from Verizon to VADI.

8. Upon completion of the foregoing 2 steps, VADI shall seek cancellation of its Certificate of Public Convenience and Necessity.

9. As a condition of the transfer, Verizon and VADI shall jointly notify customers of the transfer and make clear that these customers are not required to take advanced services from Verizon/VADI, except to the extent that customers are subject to a term commitment pursuant to a contract or under the applicable tariff.

10. Verizon and VADI shall prepare a joint notice explaining this decision to customers, and submit it to the Commission's Public Advisor for review and approval prior to mailing, and mail the notice to all customers - as a separate mailing or a bill insert - at least 10 business days before effecting the asset transfer.

11. In its compliance advice letter filing due within 60 days of the effective date of this decision, VADI may value the assets being transferred back to Verizon on a book value basis.

12. A.00-09-028 is closed.

13. A.01-11-014 shall remain open in the event there is a necessity to proceed to Phase 2 of the proceeding, but shall close automatically one year after the effective date of this decision if we have not lifted the stay of A.01-11-014 by that date.

This order is effective today.

Dated June 19, 2003, at San Francisco, California.

MICHAEL R. PEEVEY
President
CARL W. WOOD

LORETTA M. LYNCH
GEOFFREY F. BROWN
SUSAN P. KENNEDY
Commissioners